

Message Text

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ACTION TRSE-00

INFO OCT-01 EA-07 ISO-00 NEA-10 IO-10 H-02 L-03 PA-01

PRS-01 SP-02 AID-05 EB-07 NSC-05 CIEP-01 SS-15 STR-04

OMB-01 CEA-01 CIAE-00 COME-00 FRB-03 INR-07 NSAE-00

USIA-06 XMB-02 OPIC-03 LAB-04 SIL-01 AGR-05 /107 W

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P 240809Z OCT 75

FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 8823

INFO AMEMBASSY JAKARTA PRIORITY

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USADB

FOR NAC AGENCIES

E.O. 11652: ADS, DECLASS 1/24/76

TAGS: EAID, EFIN

SUBJECT: PROPOSED ADB LOAN - GOHOR LAMA PALM OIL PROCESSING
PROJECT AND PROPOSED TECHNICAL ASSISTANCE - SMALLHOLDER
DEVELOPMENT PROJECT (INDONESIA)

SUMMARY: ADB MANAGEMENT PROPOSES \$11.3 MILLION EQUIVA-
LENT LOAN FROM ORDINARY CAPITAL RESOURCES AND \$161,000
TECHNICAL ASSISTANCE (TA) GRANT TO GOVERNMENT OF INDO-
NESIA. LOAN TO FINANCE FOREX COST OF (I) CONSTRUCTION
OF GOHOR LAMA MILL FOR PROCESSING OIL PALM WITH RELATED
TRANSPORT AND INFRASTRUCTURE FACILITIES; AND (II)
CONSULTANT SERVICES. TA TO FINANCE CONSULTANT SERVICES
FOR PREPARATION OF FEASIBILITY STUDY ON INSTITUTIONAL
AND TECHNICAL ASPECTS OF SMALLHOLDER DEVELOPMENT PROJECT
IN ADJACENT AREA. USADB RECOMMENDS FAVORABLE NAC ACTION.
END SUMMARY.

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1. ABD COC. R97-75 WITH ATTACHMENTS DESCRIBING PROPOSED

LOAN AND GRANT POUCHES ADDRESSEES OCTOBER 21. BOARD
CONSIDERATION SCHEDULED NOVEMBER 6, 1975.

2. ADB MANAGEMENT PROPOSING \$11.3 MILLION LOAN FROM ORDINARY CAPITAL RESOURCES AND \$161,000 TA GRANT TO GOVERNMENT OF INDONESIA. PROCEEDS OF LOAN WILL FINANCE FOREX COST OF CONSTRUCTION OF GOHOR LAMA PALM OIL PROCESSING MILL LOCATED IN NORTH SUMATRA, ABOUT 65 KM. NORTHWEST OF PROVINCIAL CAPITAL OF MEDAN, WITH RELATED TRANSPORT AND INFRASTRUCTURE FACILITIES INCLUDING CONSTRUCTION OF RAILWAYS, ROADS AND PROVISION OF TRANSPORT EQUIPMENT; AND CONSULTANT SERVICES AND TRAINING OF TECHNICAL PERSONNEL. PROCEEDS OF TA GRANT WILL FINANCE FEASIBILITY STUDY FOR FURTHER DEVELOPMENT OF AN OIL PALM NUCLEUS ESTATE FOR SMALLHOLDERS IN AREA ADJACENT TO EXISTING PALM OIL ESTATE AND PROPOSED MILL TO BE FINANCED UNDER LOAN PROJECT. PROPOSED LOAN TERMS ARE 20 YEAR AMORTIZATION INCLUDING 4 YEAR GRACE PERIOD, 8-3/4 PERCENT INTEREST, REPUBLIC OF INDONESIA TO BE BORROWER AND PERUSAHAAN NEGARA PERKEBUNAN II (PNPII), A STATE ESTATE ENTERPRISE UNDER MINISTRY OF AGRICULTURE, TO BE EXECUTING AGENCY. LOAN PROCEEDS TO BE RELENT TO PNPII ON SAME AMORTIZATION TERMS BUT WITH 15 PERCENT INTEREST RATE, WHICH IS GOVERNMENT'S PREVAILING RELENDING RATE. RE TA GRANT, IF LOAN PROJECT IS FORMULATED AND BANK LOAN SUBSEQUENTLY APPROVED, AMOUNT OF TA EXCEEDING \$100,000 WILL BE INCORPORATED IN SUCH LOAN IN ACCORDANCE WITH STANDARD BANK POLICY. EXECUTING AGENCY FOR TA TO BE DIRECTORATE GENERAL OF ESTATES (DGE) IN MINISTRY OF AGRICULTURE.

3. AGRICULTURE IS FOUNDATION OF INDONESIAN ECONOMY. IN 1973/74 IT ACCOUNTED FOR 60 PERCENT OF TOTAL EMPLOYMENT, 40 PERCENT OF GDP AND 43 PERCENT OF EXPORTS. PLANTATION AGRICULTURE PLAYS SIGNIFICANT ECONOMIC ROLE. EXCEPT FOR OIL PALM, ALL PRINCIPAL ESTATE CROPS -- RUBBER, COFFEE, TEA, SUGARCANE, FIBERS, AND TOBACCO -- ARE GROWN BY BOTH ESTATES AND SMALLHOLDERS. IMPORTANCE OF PLANTATION SECTOR, PARTICULARLY ITS POTENTIAL FOR INCREASED EXPORT EARNINGS OR IMPORT SUBSTITUTION, IS CLEARLY RECOGNIZED BY GOVERNMENT.

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4. IN 1973, INDONESIA PRODUCED ABOUT 290,000 TONS OF PALM OIL (OF WHICH 249,000 TONS WERE EXPORTED), AND 30,000 TONS OF PALM KERNEL OIL. EXPORTS HAVE INCREASED BY 41 PERCENT SINCE 1966. OVER NEXT DECADE, WORLD DEMAND FOR VEGETABLE OILS INCLUDING PALM OIL IS EXPECTED TO INCREASE EVEN FASTER THAN RAPID GROWTH ANTICIPATED FOR FATS AND OILS IN GENERAL. TO MEET PROJECTED WORLD DEMAND FOR

PALM OIL, MORE THAN 60 PERCENT INCREASE IN WORLD PRODUCTION IS ANTICIPATED BETWEEN 1973 AND 1980.

5. ADB HAS MADE TWO PREVIOUS LOANS TO INDONESIA FOR PALM OIL PROJECTS: \$2.4 MILLION FOR SAWIT SEBARANG OIL PALM ESTATE (1969) AND \$7.41 MILLION FOR NORTH SUMATRA RUBBER AND OIL PALM (1971). IN DECEMBER 1973, BANK REVIEW MISSION FOUND THAT TWO PROJECTS HAD CONTRIBUTED TO RAPID INCREASE IN PRODUCTION OF OIL PALM FRESH FRUIT BUNCHES (FFB) AND WOULD NECESSITATE EXPANSION OF EXISTING MILLING FACILITIES IN PROJECT AREAS BETWEEN 1976 AND 1982. IN MAY, 1974, BANK APPROVED \$49,200 TA GRANT TO UNDERTAKE FEASIBILITY STUDY FOR EXPANSION OF PROCESSING CAPACITY. FOLLOWING SUBMISSION OF CONSULTANT'S RECOMMENDATIONS, BANK APPRAISAL MISSION VISITED INDONESIA IN FEBRUARY/MARCH 1975 AND FORMULATED PROJECT FOR PALM OIL PROCESSING FACILITIES AND SMALLHOLDER DEVELOPMENT. GOVERNMENT PROPOSED THAT PROJECT BE DIVIDED INTO TWO PHASES: (A) PHASE I, TO CONSIST OF PROPOSED LOAN AND TA PROJECTS; AND (B) PHASE II, TO BE UNDERTAKEN SUBSEQUENTLY BY GOVERNMENT, TO INCLUDE CONSTRUCTION OF ONE ADDITIONAL PALM OIL MILL AND SMALLHOLDER DEVELOPMENT EXPECTED TO RESULT FROM PHASE I FEASIBILITY STUDY. COMPLETION OF GOHOR LAMA PROCESSING MILL CONSTRUCTION PLANNED BY END OF 1977. COMPLETION OF PHASE II PALM OIL MILL ANTICIPATED IN 1980/81.

6. TOTAL COST OF GOHOR LAMA PROJECT ESTIMATED AT \$15.6 MILLION, INCLUDING 10 PERCENT FOR CONTINGENCY AND 26.4 PERCENT FOR PRICE ESCALATION. PROPOSED BANK LOAN WOULD COVER \$11.3 MILLION EQUIVALENT FOREX COST. GOVERNMENT WILL RAISE \$4.3 MILLION LOCAL COST REQUIREMENT BY EXEMPTING EXECUTING AGENCY FROM PAYMENTS TO NATIONAL DEVELOPMENT FUND AND FROM PAYMENTS OF DIVIDENDS TO GOVERNMENT. LIMITED OFFICIAL USE

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PROPOSED LOAN PROVIDES FOR (A) CONSTRUCTION OF ONE PALM OIL MILL (INCLUDING ANCILLARY FACILITIES AT GOHOR LAMA; (B) CONSTRUCTION OF ABOUT 2.8 KM. OF NARROW-GAUGE TRACKS AND PROVISION OF MAINTENANCE EQUIPMENT FOR NARROW-GAUGE RAILWAY NETWORKS; CONSTRUCTION OF ABOUT 2.8 KM. OF NORMAL-GAUGE TRACKS AND PROTECTION OF RIVER BANKS OVER BATANG SERANGAN RIVER; (C) GRAVELLING OF ABOUT 375 KM. OF PLANTATION ROADS INCLUDING PROCUREMENT OF CONSTRUCTION AND BT

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ACTION TRSE-00

INFO OCT-01 EA-07 ISO-00 NEA-10 IO-10 H-02 L-03 PA-01

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USIA-06 XMB-02 OPIC-03 LAB-04 SIL-01 AGR-05 /107 W

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P 240809Z OCT 75

FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 8824

INFO AMEMBASSY JAKARTA PRIORITY

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MAINTENANCE EQUIPMENT; CONSTRUCTION OF ABOUT 3 KM. AND REHABILITATION OF ABOUT 16 KM. OF CONNECTING ROADS AND STRENGTHENING OF THREE BRIDGES; (D) PROVISION OF RAIL EQUIPMENT FOR TRANSPORT OF FFB, OIL AND KERNELS AND ROAD EQUIPMENT FOR FFB TRANSPORT; CONSTRUCTION OF PALM OIL BULK STORAGE INSTALLATIONS AT BELAWAN PORT; AND (E) CONSULTING SERVICES FOR CONSTRUCTION SUPERVISION AND TRAINING OF TECHNICAL PERSONNEL, FELLOWSHIPS AND TRAINING ABROAD.

7. ON MAY 23, 1975, BANK MANAGEMENT INFORMED BOARD (DOC. IN.58-75) THAT TGANCE PROCUREMENT ACTION WOULD BE TAKEN, WITHOUT PRIOR COMMITMENT FOR BANK FINANCING BUT IN ACCORDANCE WITH BANK PROCEDURES, IN ORDER ACHIEVE MILL COMPLETION BY END 1977 TO PREVENT FFB LOSSES DUE TO INSUFFICIENT PROCESSING FACILITIES. CONSULTANT SER-

VICES FOR BID EVALUATION BEING FINANCED FROM PNPII'S OWN RESOURCES. TENDERS WERE OPENED SEPTEMBER 15 AND ARE LIMITED OFFICIAL USE

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CURRENTLY BEING EVALUATED. BECAUSE OF COMPLEXITY OF MILL SYSTEM AND EXECUTING AGENCY'S LACK OF EXPERIENCE IN SUCH MAJOR PROJECT, MILL WILL BE PROCURED AND CONSTRUCTED ON TURNKEY BASIS AND WILL INCLUDE ENGINEERING, SUPPLY OF EQUIPMENT AND CONSTRUCTION OF CIVIL WORKS BY ONE FIRM. THIS CONTRACT AND OTHER PROCUREMENT CONTRACTS OF \$100,000 EQUIVALENT OR MORE TO BE AWARDED ON BASIS INTERNATIONAL COMPETITIVE BIDDING. CONTRACTS LESS THAN \$100,000 TO BE AWARDED ON BASIS BIDS OR QUOTATIONS FROM REASONABLE NUMBER OF SUPPLIERS FROM MORE THAN ONE ELIGIBLE COUNTRY.

8. TWO CONSULTANTS WILL BE RECRUITED IN ACCORDANCE WITH BANK'S GUIDELINES TO ASSIST WITH SUPERVISION OF MILL ERECTION AND TECHNICAL STAFF TRAINING. SUPERVISORY CONSULTANT TO BE PROVIDED FOR 5.5 MAN-MONTHS, WHILE TRAINING CONSULTANT'S TERM WOULD BE TWO YEARS FROM 1976 TO 1977 BEFORE MILL BECOMES OPERATIONAL. PROJECT ALSO PROVIDES FOR VISIT BY CHIEF/MILL ENGINEERS TO VISIT PRINCIPAL SUPPLIERS OF EQUIPMENT FOR TRAINING, IN ADDITION TO THEIR RECEIVING FURTHER CONTRACTOR ASSISTANCE DURING FIRST YEARS OF PRODUCTION.

9. PROPOSED TA GRANT WOULD FINANCE \$161,000 FOREX COST OF FEASIBILITY STUDY FOR FURTHER DEVELOPMENT OF OIL PALM NUCLEUS ESTATE FOR SMALLHOLDERS. LOCAL COST OF \$50,000 EQUIVALENT TO BE BORNE BY GOVERNMENT. STUDY, WHICH GOVERNMENT INTENDS TO UTILIZE SUBSEQUENTLY FOR OTHER SUCH PROJECTS, WOULD DETERMINE FEASIBLE ALTERNATIVE DEVELOPMENT OPTIONS AND DEVELOP CRITERIA FOR SELECTION OF OPTIMUM PROPOSAL. IT WOULD ALSO FORMULATE MOST ADVANTAGEOUS SMALLHOLDER DEVELOPMENT PROJECT PROPOSAL FOR POSSIBLE BANK FINANCING TO INCLUDE LAND CLEARING, PLANTING OF OIL PALM, CONSTRUCTION OF SERVICE ROADS, VILLAGE INFRASTRUCTURE FOR SETTLEMENT OF ABOUT 1,500 FAMILIES, INSTITUTIONAL ARRANGEMENTS FOR SMALLHOLDER DEVELOPMENT, CONSULTING SERVICES AND TRAINING. CONSULTANT TEAM FROM EXPERIENCED FIRM TO BE UTILIZED FOR SIXTEEN MAN-MONTHS AND COMPOSED OF AGRONOMIST EXPERIENCED IN SMALLHOLDER DEVELOPMENT, PHYSICAL PLANNER, INSTITUTIONAL EXPERT AND AGRICULTURAL ECONOMIST.

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10. TO ENABLE PNPII TO PERFORM SATISFACTORILY AS EXECUTING AGENCY FOR LOAN PROJECT, PNPII WILL MERGE WITH PNP SAWIT SEBARANG, A FINANCIALLY INDEPENDENT STATE ESTATE ENTERPRISE SET UP EARLIER TO OPERATE ADB-FINANCED SAWIT SEBARANG OIL PALM ESTATE PROJECT. TWO ENTERPRISES WILL BE CONVERTED INTO LIMITED LIABILITY COMPANY UNDER INDONESIAN COMMERCIAL CODE (PT), WHICH WILL BE PRE-CONDITION OF PROPOSED LOAN EFFECTIVENESS. BANK MISSION INDICATES THAT NEW PT'S OVERALL FINANCIAL SITUATION IS PROJECTED TO BE BASICALLY SOUND AND PROFITABILITY SATISFACTORY. MISSION ALSO CONSIDERS DGE, THE EXECUTING AGENCY FOR TA, TO BE WELL EXPERIENCED TO ASSUME NECESSARY RESPONSIBILITIES.

11. BANK CONSIDERS PROPOSED LOAN PROJECT TO BE WELL CONCEIVED, TECHNICALLY FEASIBLE, FINANCIALLY VIABLE, ECONOMICALLY SOUND AND LOGICAL FOLLOW-UP TO EARLIER BANK-FINANCED PROJECTS IN THIS SECTOR. OBJECTIVE OF MERGER OF TWO PNPS INTO LIMITED LIABILITY COMPANY SEEKS TO ESTABLISH ECONOMIC AND FINANCIAL PERFORMANCE CRITERIA FOR SUCH GOVERNMENT ENTERPRISES. FOREX EXPORT EARNINGS TO BE DERIVED FROM PROJECT WILL ASSIST GOVERNMENT IN EXPANDING NON-PETROLEUM SECTOR EXPORTS. (ANNUAL NET FOREX EARNINGS ESTIMATED AT \$6.1 MILLION.) ECONOMIC AND FINANCIAL RATES OF RETURN ARE ESTIMATED AT 20.0 PERCENT AND 13.9 PERCENT, RESPECTIVELY. PROPOSED TA IS IN LINE WITH GOVERNMENT POLICY OF ENCOURAGING THAT BENEFITS OF ECONOMIC DEVELOPMENT ARE WIDELY SHARED. USADB SUPPORTS PROPOSAL AND RECOMMENDS FAVORABLE NAC ACTION.

12. REQUEST JAKARTA'S COMMENTS FOR NAC AGENCIES, INFO USADB MANILA, PURSUANT TO STATE 119795 DATED 3 JULY 1972. SULLIVAN

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Message Attributes

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Draft Date: 24 OCT 1975
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Disposition Approved on Date:
Disposition Authority: CunninFX
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
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Handling Restrictions: n/a
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TAGS: E AID, EFIN, RP, ADB
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Type: TE
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